RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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JULY 6, 2000 **LETTER 1303**

June 16, DJIA 10449.30; PTI 5129; A-D Ratio -6.38
June 23, DJIA 10542.99; PTI 5120; A-D Ratio -6.87
June 30, DJIA 10447.89; PTI 5120 ; A-D Ratio - 6.55
Dow Yield: 1.60%; Dow Price/Earnings: 20.5
Dow Times Book Value: 6.18%
Percentage of Undervalued Blue-chips: 14%
Gold 34-day MA: 287

THE PICTURE: I said it on my Internet site, but I want to say it again. "Find something you love, and you'll never work another day in your life."

It's true. And people ask, "Russell, when are you going to retire?" I answer, "Retire to what? To boredom? No thanks, I like what I'm doing."

Then people ask me, "Richard, you've been writing your stuff for 43 straight years without ever missing a single issue. Why don't you take a nice long vacation?" And I answer, "Yeah, I've thought about it -- the only trouble is that I like what I'm doing more than I like vacations."

To me the markets and my "Notes & Quotes" and my daily web site keep me in touch with the world. I love to read the *New York Times* in the morning, I love to read the *Wall Street Journal* when I get up at 4 a.m. (we get early delivery here), I love to check stories on the Internet, and I love to see what Globex is doing at 1 a.m. I'm a nut, I admit it, but I like my life. I love my kids, I love my wife, I love my two standard poodles, I love La Jolla (even though it's getting crowded), and I love the weather here. So no, I don't need a vacation. A vacation takes me away from where I want to be. I'm happy here, just working.

Freud said, "Love and work, that's all there is." Believe it.

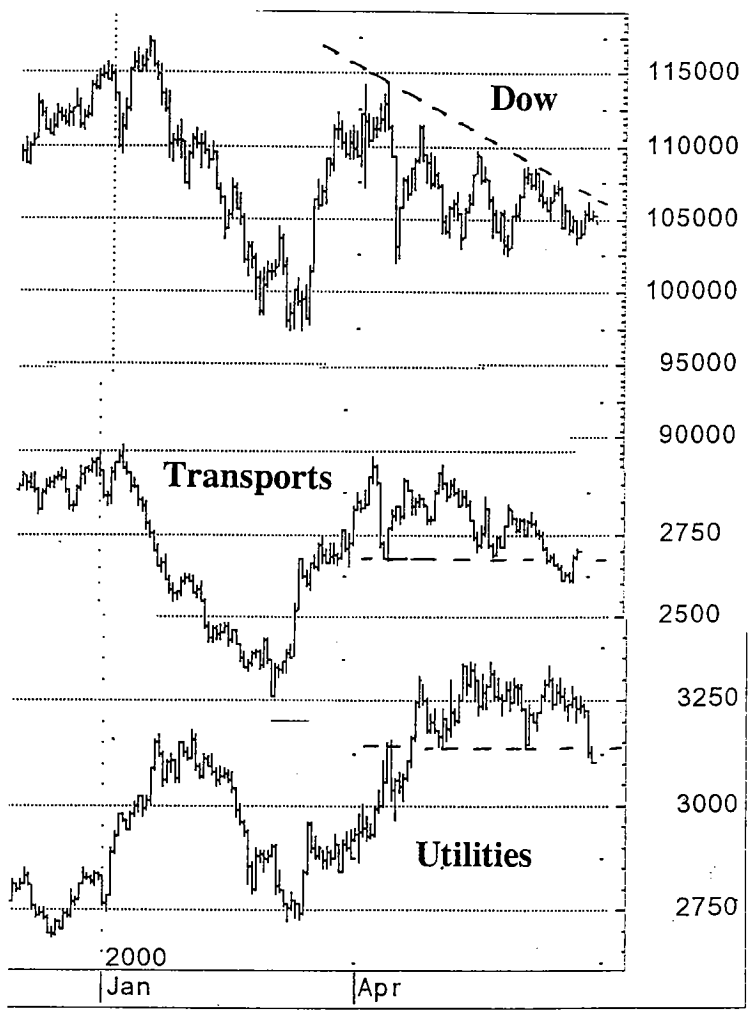
OK, let's move on to more important things than just what keeps Richard Russell going. Such as what the markets are doing. By early June the market got very over-bought. How do I know that? I just check the McClellan Oscillator, which is the difference between two exponential averages of the advance-decline line (the McClellan can be monitored daily on www.decisionpoint.com ($10 a month and well worth it). According to some authorities, the market has become very "Darwinian." By that they mean that the strongest stocks are taking over, while the weaker stocks are falling by the wayside. An Intel climbs while ten lesser tech stocks sink ignominiously. In due time, say these experts, a selected group of leading stocks will rule the business world while the great mass of stocks, as monitored by the advance-decline ratio, will sink into the misty clouds of history.

Will the Darwinian approach negate the thesis of primary bull and bear markets? I sincerely doubt it, but only time will tell. In the meantime, I want to include my updated, enlarged and corrected "Top Out Parade" (a few items have been added and a few have been corrected through help from my subscribers, who, by the way, miss nothing). It will be important to see if any of these "milestones" can be bettered in the period ahead.

TOP OUTS

Daily new highs topped out at 631 on October 3, 1997.

The advance-decline ratio topped out on April 3, 1998 at 13.00.



The Value Line (geometric) topped out on April 21, 1998 at 508.39.

The Morgan Stanley Cyclical Index topped out on May 10, 1999 at 619.09.

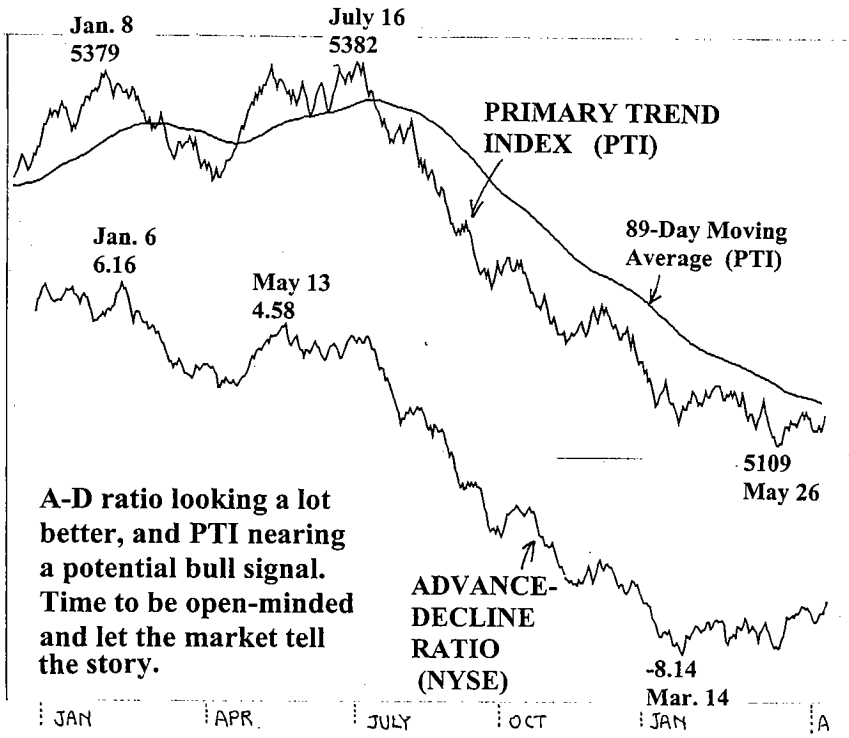
The D-J Transportation Average topped out on May 12, 1999, at 3783.50.

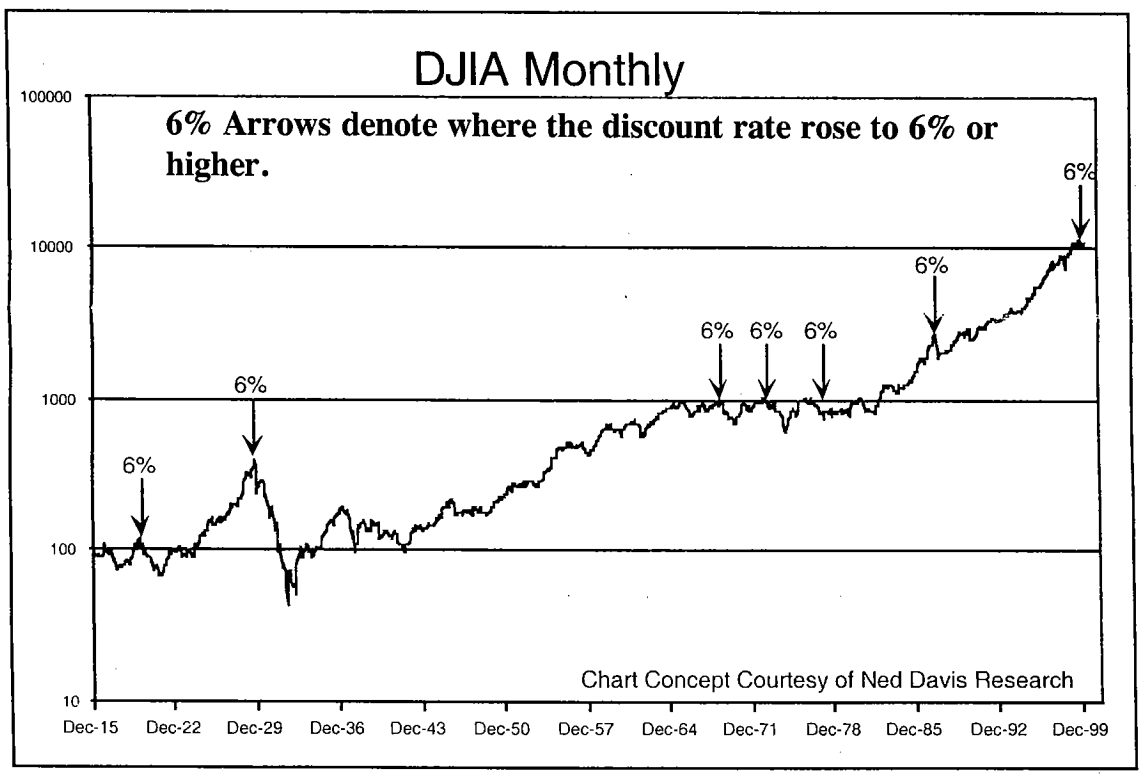
The NYSE Financial Average topped out on May 13, 1999 at 584.21.

The D-J Utility Average topped out on June 16, 1999 at 333.45.

The NYSE Composite topped out on July 16, 1999 at 663.12.

The D-J Industrial Average topped out on January 14, 2000 at 11722.98





The Russell 2000 topped out on March 9, 2000 at 606.05.

The Nasdaq topped out on March 10, 2000 at 5048.62

The Amex Index topped out March 23, 2000 at 1036.40.

The Wilshire 5000 topped out on March 24, 2000 at 14751.64.

The S&P topped out on March 24, 2000 at 1527.46.

On this page I am including a chart courtesy of Peter Eliades' very fine service, *Stockmarket Cycles* (800-888-4351). This chart is based on data from Ned Davis Research. It shows the six previous instances in history when the discount rate rose to 6% or more, plus the most recent rise to a 6% discount rate.

The dates of the six previous discount rate increases to at least 6% were Jan. 23, 1920; Aug. 9, 1929; Apr. 3, 1969; Apr. 11, 1973; Oct. 26, 1977 and Sept. 4, 1987. The most recent boost to a 6% rate occurred on May 16, 2000.

In every case around or following the 6% (or more) discount rate the market ran into trouble, sometimes lesser trouble such as in 1969 and sometimes major trouble such as in 1929 and in 1973. But in every case, a rise to a 6% discount rate was associated with a rotten stock market.

Will it be any different this time? I doubt it, particularly since the latest boost to 6% came within the context of a primary bear market and in the face of the most overvalued market in history.

On the first page I show a chart of the three D-J Averages.

First, the Industrial Average -- following the April peak we see a series of six rallies, each rally ending below the peak of the preceding rally. To me, this spells weakness in the Dow. The important "support" area for the Dow comes in at 10200. If that level is broken, the Dow will probably test its bear market low of 9796.03.

The Transportation Average rallied to a secondary peak on April 12 at 2952.63. Since then the Average has weakened, and most recently it has violated two preceding lows. Last week, we had another Transport rally, but the "look" of the Transportation Average is weak.

Finally, we see the Utility Average, an average which many times in the past has acted as a bellwether (usually with a longish lead time). At any rate, on May 11 the Utility Average advanced to within a fraction of its record high. But surprisingly, since then, the Average has traced out a "head-and-shoulders top" pattern. Last week the Utility Average broke down through its support at 315. I'm not sure what this means, but I know one thing -- it's not a plus for the stock market.

On the web site a few weeks ago I talked about parabolas in individual stocks and in indices, and I said that I would illustrate parabolic patterns in some current stock patterns.

A parabola is an accelerating pattern in which the item moves higher and higher until it culminates in an almost vertical climb. The final vertical climb reflects a frenzy to buy and a climactic surge of enthusiasm and bullishness. As a rule, once the final vertical climb crests, the move is over. The upside is exhausted, and a long bear market in the item begins.

On page 3 and 4 I include a random selection of stocks in parabolic patterns, courtesy of www.decision point.com.

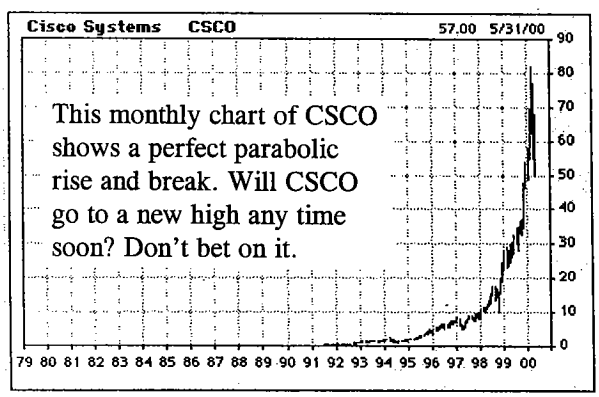
INVESTMENT POSITION: Yep, the bear is still in the box. Buying good stocks for the long term is known as **investing.** The problem with investing in stocks now is that they're just plain **overvalued.** At previous major bull market tops the S&P sold for around 20 or less times record earnings. The problem now is that the S&P is selling for 28 times record earnings.

Over the short term the market can do anything and usually does. **But over the long term values rule,** and serious investors know this. Which is why serious investors are more apt to sell this market than buy it. And that's why when you buy a package of stocks here, after six months or a year or two the odds are that you'll be losing money. It's as simple and fundamental as that.

Sure there's the hype and the excitement as one group or another rallies in this first phase of the bear market. But beneath the hype, stocks are being distributed by seasoned investors who know that at 28 times record earnings the market is building a massive top.

Meanwhile, stocks and groups run up and run down, but it's all speculation, not investing. And the real money is made in investing, not speculation. As a matter of fact, for the non-professional, speculation usually ends up in losses.

For that reason and for the reason that this is a bear market I've been advocating caution, a lot of caution. I'll tell you what -- if you don't know what to do or where to put your money, let me suggest two to three year Treasury notes. You'll get around 6.4% on your money, you won't pay state taxes, and you'll sleep well (unless you're like me, in which case you'll get up at 1AM, watch some TV and then go back to sleep around 2AM, but you won't worry about whether Hot-tech.com which you just bought is going to fall out of bed tomorrow at the opening).


Cisco Systems CSCO
57.00 5/31/00
This monthly chart of CSCO shows a perfect parabolic rise and break. Will CSCO go to a new high any time soon? Don't bet on it.
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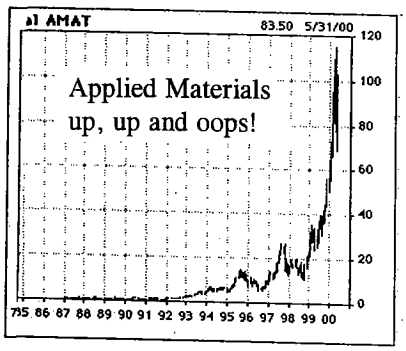

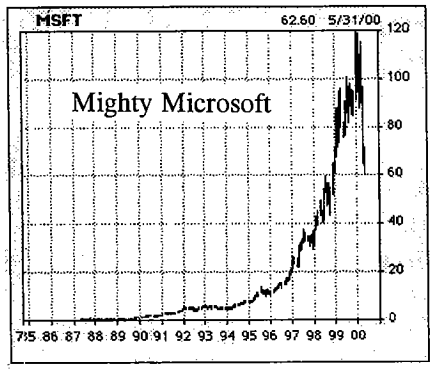

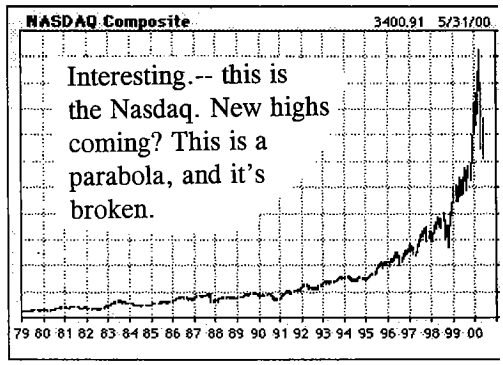

NOTES & QUOTES: -- Microsoft: "Did the Giant Slay Itself? Microsoft's mistake was to treat the government as if it were just another competitor, critics say." So said the *Washington Post* weekly (June 12). And famous last words from Bill Gates, "This antitrust thing will blow over." Continues the *Washington Post:* There will be many rich areas of scholarly exploration. Can the roots of the breakup be ultimately traced to Gate's longtime attitude that competitors should not be merely beaten but put out of business? Could the company have been saved with any courtroom approach other than one that even its sympathizers say was sometimes bumbling and always fatally arrogant?

As one expert put it, "It wasn't so much that the Dept of Justice won the trial. Microsoft lost it. It's like going in for a speeding ticket and coming out with a death sentence."

Writes Thomas Friedman, columnist in the *New York Times:* "As far as I'm concerned, the government has grounds to break up Microsoft simply for what Mr. Gates did last year -- which was to hire an army of lobbyists to try to get Congress to cut the budget of the antitrust division of the Justice Dept. while Microsoft's case was underway. Think about the arrogance behind that. How would you feel if the biggest company in your town tried to have the police department funding slashed at a time when the police were bringing charges against it? That's what Microsoft did."

Russell Comment: Corporate culture is almost always a reflection of the man at the top. Gates, brilliant, coming from a wealthy family, was a perfect example of Lord Acton's dictum that "All power corrupts and absolute power corrupts absolutely." Gates became not only the richest man in the world but power-mad. He thought he could beat the world, and in the end nobody can. Personally, I don't give a damn whether MSFT remains an entity or whether it will be broken up into 40 divisions. Gates' power will never be the same. The world has seen through him. The emperor still has clothes, but they don't fit right anymore. In fact, they look sort of seedy.

* *

Last time I was in NY, which was a couple of years ago, I ate at the Union Square Cafe which is arguably the best restaurant (foodwise) in NY. Nearby is the Greenmarket, in which farmers bring their wares along with flower-growers, etc. The Farmers pay $62 a day for their spots and they must sell ONLY what they have produced. Says Michael Romano, chef at the Union Square, it was an important reason why we set up shop at this neighborhood 15 years ago. "We wanted to be near a source of great food, to stay in tune with the seasons."

* *

You think my life is all dullness and drudgery? Wrong! Here's a photo of your editor at a party given by daughter, Betsy, in LA. The lady on my right is Farrah Fawcet. The lady on my left is actress Nicolette Sheridan. It's almost embarrassing -- these Hollywood beauties just won't leave me alone. What's my secret? Obviously, it's the Fu Manchu mustache.

* *

Water: It happened in California. A court decision blocked construction of new homes at Newhall Ranch unless it can be demonstrated that they have assured water sources. The developer must have a 50-year source of water locked in before it can start work on the first of 22,000 homes. It is felt that this demand will push up water prices in Southern California. It is also thought that this is a peek at the future of Southern California. Water -- there's just no substitute for it.

* *

Finally, they're doing it. Boeing in 2002 will launch an unmanned 35-foot scale model of a revolutionary "blended

wing body" aircraft which will be developed with the National Aeronautics and Space Administration. This will herald the flying wing. The flying wing has been proved to have dramatically superior aerodynamics than the current "tube with attached wing." The flying wing is an idea that my pal, Harry Schultz, has been pushing for years and years. Harry, maybe, just maybe the flying wing has arrived.

In the meantime, Airbus (composed of four European partners) gave the go-ahead for AaXX, a jumbo jet that will carry between 481 and 656 passengers in the world's largest civil aircraft. The AxXX will cost about $12 billion to develop and it is hoped that it will break the 30-year monopoly enjoyed by Boeing. The AaXX is expected to fly in 2004 and enter service in 2005. The system will employ 160,000 workers in Europe and possibly 50,000 more elsewhere. To compete, Boeing has announced a stretched version of its 747 which will seat more than 500 passengers.

* *

Cracking the human genetic code is one of the greatest and most fantastic feats in the history of science. This is the *Washington Post's* description of Celera's lab. "Inside Celera's sequencing labs, glass-enclosed robots the size of small cars tirelessly process pieces of human DNA seven days a week, 24 hours a day, allowing 45 technicians to do the work of 1,000 as the company races to assemble the genome in final form. Supercomputers conduct genetic analyses day and night in cavernous air-conditioned rooms, running up electric bills of $1 million a year. The company's headquarters is threaded with 400 miles of wiring, half of it high-capacity fiber optics. And to serve the pharmaceutical companies and other scientific subscribers that are already paying for access to its data, Celera sports a computer as big as America Online's."

* *

The dot.coms will have to change if they're to survive. If you want to get financing, the new rule is P2P or path to profits. Venture capitalists now look for real business plans, they want profitability within a year after the public offering, and if you're trying to sell an e-tailer or a site that provides only content, you can forget it, the venture capitalists will almost surely not be interested. As a result, many dot.coms that need additional money are now going to private sources to raise it. Morgan Stanley tracks 377 IPOs, and they state that almost half of them are now below their IPO prices and the average is off two-thirds from its 52-week high.

* *

By the way, the following companies have dropped off *Business Week's* IT (Information Technology) 100 listing: Amazon.com; IBM; Intel; Qualcomm; Ebay; Qwest; Lucent Technologies; Ameritrade. All top names, but *Business Week* gives their reasons why each one dropped off their favored list.

* *

I received a report from a subscriber who wants to know how I can say that the national debt is rising while the government at the same time claims that it's running a surplus. The process of compounding the national debt means that the debt continues to grow, and the government surplus isn't large enough to counter-act the compounding cost of servicing the debt. Thus the figures show that the national debt is indeed growing, despite this year's surplus in the budget (the so-called surplus which is aided by money taken from Social Security). The latest figures show that over the last 12 months $100 billion has been added to the national debt.

* *

One of the gimmicks of this market is the issuance of millions of options. Instead of paying huge salaries to employees, they were given options. But since options are a potential source of additional stock and therefore can "water" a stock, corporations counter-act this by buying their stock back.

But what happens when employees are given stock options and the company's stock caves in, rendering the options almost worthless? The company has three choices: (1) Do nothing and take a chance of losing its employees. (2) Issue more options at a lower price. (3) Re-price its options, a practice now frowned upon by accountants.

* *

Notes: Microsoft has issued 70 million additional options to make up for its sliding stock price. Interestingly, if MSFT's employees exercised just half of the options recently issued, MSFT would have to spend $3.7 billion to repurchase the shares, and this equals half of MSFT's 1999 earnings. . . At latest count, options outstanding are equal to 16% of all common stocks outstanding, which is a new high percentage. And it's a huge potential watering of stock outstanding.

* *

IBM has been spending billions to retire shares and thereby move its per-share earnings up. In the meantime, however, its debt has increased by $6 billion to $28 billion, with its debt now 59% of its total capitalization. IBM will soon have to find some other way of increasing its per share earnings, like maybe increasing sales.

* *

The hottest car now is Chrysler's PT Cruiser. This cute little retro four cylinder car has created the most buzz since the new Beetle was introduced. Everyone wants a Cruiser. So far 80,000 people have signed up for a Cruiser, some paying $4000 over list. It's the first car out this year that people can actually recognize. The design mimics the cars of the late 1930s. It's small, it's cute, it's different, and it's well -- anti SUV. Daimler-Chrysler has now quadrupled production on this scaled-down mini-van. Are high-priced gas and low-priced cars "in"? Could be.

* *

2000 dust bowl? You may not know it if you live in a big city but parts of the nation are now experiencing a huge

drought--and I'm referring to the Midwest, the Southwest and the West. Sections of Florida, Georgia, Mississippi and Louisiana have edged close or have posted their driest six months (through May) since 1895. For parts of Iowa, Texas, Nebraska and Missouri the same is true for an 11-month period. Here in Southern California I can't remember when we had the last real rain. Even my Cacti are unhappy.

* *

It may not mean much to you East-coasters, but to us just 20 miles north of the border the Mexican election this week was of great interest. The domination of the PRI party is over, and Vincente Fox, a former Coca-Cola executive who galvanized Mexico with his cries for change, has just been elected -- the nation's first opposition president in 71 years. Fox heads PAN or the National Action Party. All Mexico is celebrating the new president, and you can practically hear the shouts here in La Jolla, half an hour from the border.

* *

In the meantime, my old friend, Harry Browne, was elected the presidential candidate of the Libertarian Party. Harry has written a dozen books, his most famous being "How I Found Freedom in an Unfree World." Says Harry, "We're the only political party that's offering to set you free."

Russell Comment: Believe it. The Libertarian Party has a 12-point platform including eliminating the income tax, eliminating Social Security and jettisoning both the "war on drugs" and federal welfare. What would happen if all this occurred? In my opinion, the nation would be a lot better off. Let me put it this way, aside from defense and domestic policing including the courts, I don't think that there's anything that the government does which couldn't be done better by the private economy.

* *

Tracking stocks -- what are they? These stocks track a division (usually a faster-growing division) of a company. AT&T in April issued their own tracking stock (AWE) which tracked their wireless division. So far, it's been a dog. It was the largest public offering ever at $10.6 billion and was offered at 29.5. On Monday AWE sold for 26 ½.

Tracking stocks, unlike regular common stocks, do not represent ownership in the corporation nor do they enjoy voting rights. They do participate in cash dividends in the division, assuming there are any dividends. I see tracking stocks as a sort of option on a division of a company. In general, I don't like them, since I don't know what the devil they really represent except a fuzzy form of speculation.

* *

Speaking of speculation, the "next big thing" may be options on individual stocks. This takes us back to the "bucket shops" of the 1920s where you could go into one of these outfits and bet on a stock by putting up a small percentage of the cost of the stock. After the crash of '29 bucket shops were outlawed. But a good gambling concept never lies dormant for long. If betting via single-stock options comes in, we'll be back to something akin to the old bucket shops. Of course, the exchanges will say that single-stock options make for increased liquidity. Yeah, right.

GOLD: How does it go, "If you can't say anything good about a person, don't say anything." How about an industry? OK, I'll say something good about gold or at least about two gold stocks. Franco-Nevada (FN.TO) listed on the Toronto exchange in Canadian dollars is going to merge with Gold Fields. This will create a fine company, with virtually no debt and over $700 million in cash. It will be a low-cost gold producer, third of all gold companies in annual gold production and fourth in market capitalization ($3.7 billion).

Franco-Nevada Mining Corp. is the world's leading precious metals royalty company with a total royalty portfolio spanning 5 million acres in six countries. Gold Fields is the world's third largest gold producer having the second largest gold reserves and resources in the industry. Franco-Nevada will apply for a NYSE listing. FN.TO sells for around 17 in Canadian dollar or under 12 in US dollars.

More gold news. Battle Mountain Gold will shortly become a wholly owned subsidiary of Newmont Mining. The prize for Newmont will be BMG's Phoenix project which is considered to be one of the best gold properties in North America. BMG also owns attractive gold properties in Bolivia, Australia and Canada.

The Russell opinion is that Franco-Nevada and Newmont are "cheap" at today's prices, and owning shares in both is a worthwhile long-term holding.

So saying, let's take an unemotional look at August gold. Here we see gold having rallied above both its 34-day and 144-day MAs, which is impressive. The next upside target is to better the June 13 intra-day high of 296.50. If gold can better 296.50, the next target would be the psychologically important 300 level. Above 300 would be an important move, and it would be a move that would catch Alan Greenspan's eye. It would also give the lie to the Labor Department's contention that there's no inflation.